

Supervision in Diversity:

Enforcing Prudential Standards in the United States

Richard Hinz

The World Bank

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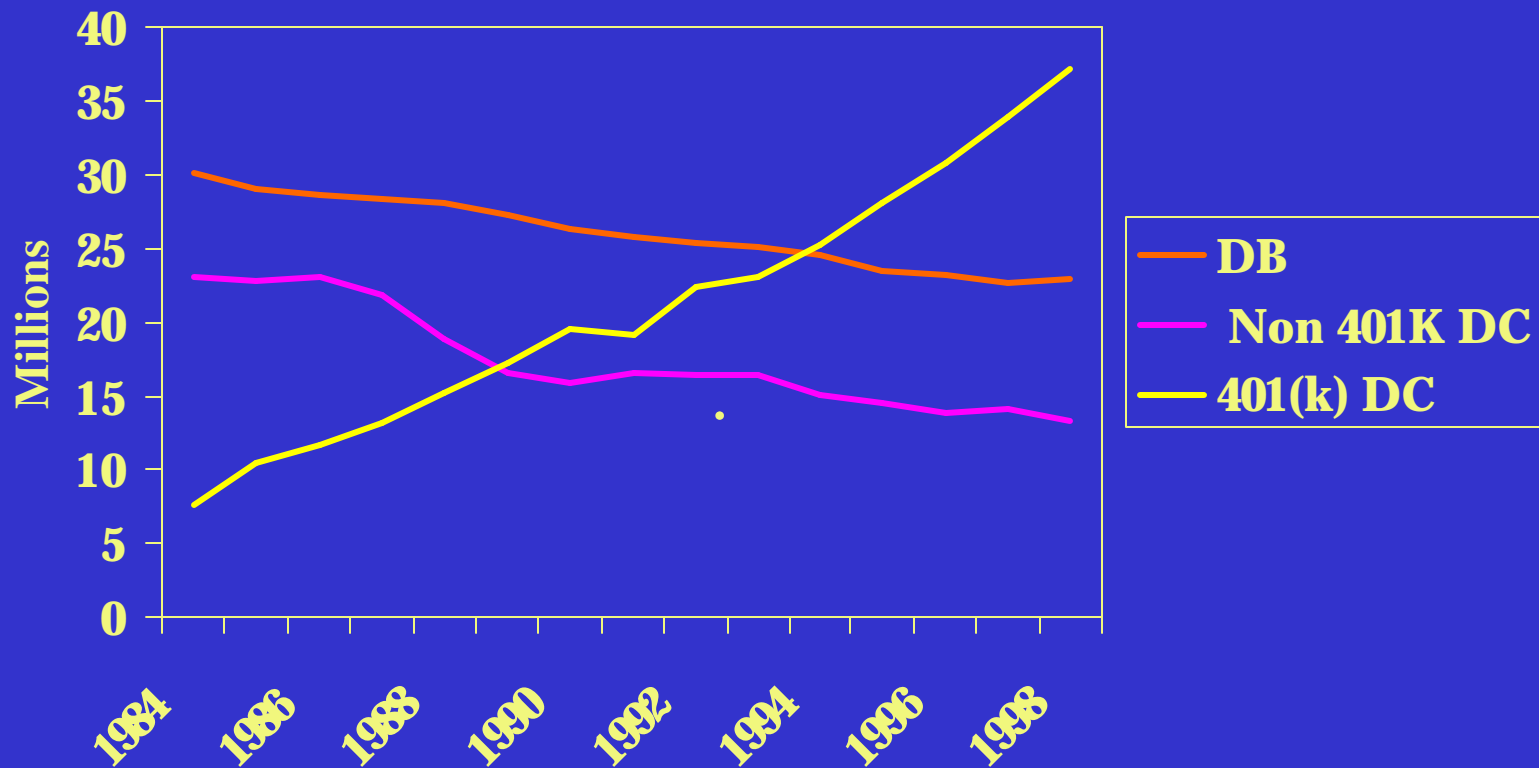
Basics of U.S. Pension System

- Voluntary employment based system
- Wide range of permissible benefit design, DB, DC and Hybrids (eg Cash balance)
- Supplements modest universal public system
 - 40% Replacement at normal retirement age for average wage, 30% actual due to early retirements
- Incentives through specific tax qualification rules
- Current coverage rate of 50% of current full time private sector workforce
 - Lifetime rates may be as much as 70%

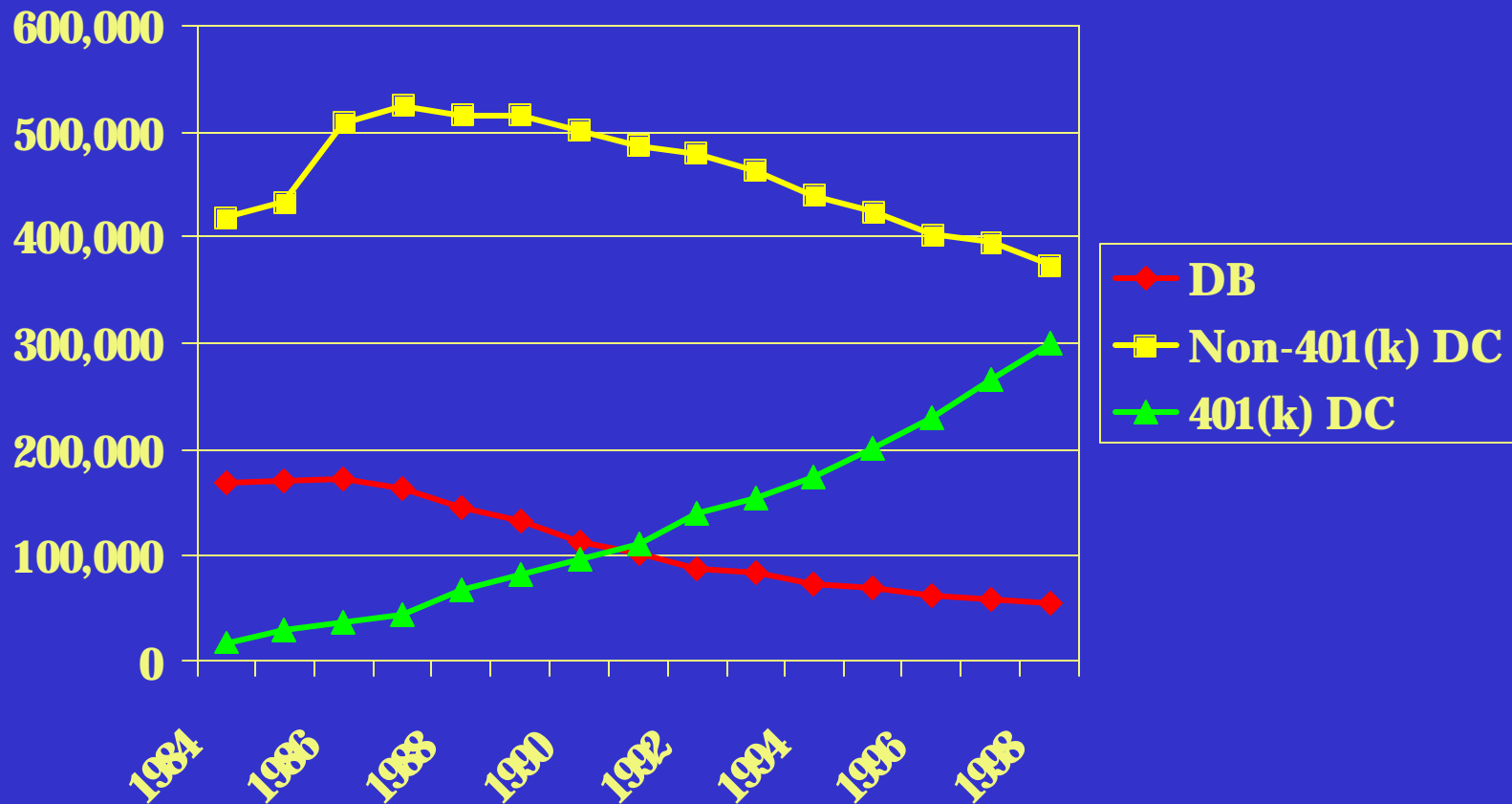
Fiduciary (Prudential) Framework

- Trust based entity
- Designated responsible individuals with ability to delegate responsibility/liability
- Adherence to written “Plan Documents”
- Prudence (diligence & expertise)
- Exclusive purpose (loyalty)
- Diversification
- Explicit prohibitions on conflict of interest and self dealing

Private Pension Plan Active Participants, 1984-1998



The Number of Private Pension Plans, 1984-1998



Regulatory Framework

- Minimal entry barriers
- Procedural (prudent person) framework
- Highly developed and regulated financial markets
- Multiple levels of financial intermediation

Structure of Supervision

- National Policy, Oversight and Evaluation Unit
- Ten Regions with Five Sub-Regions
- Groups (teams) of 8-12 staff conduct activities
- Participant Assistance Staff located in National Office and all regions

Supervision “Style”

- Re-active, Remedial, Decentralized
- Intervention on Exception Basis - Weak legal authority for pre-emptive actions
- No legal authority for punitive or compensatory sanctions
- Emphasis on negotiation based settlements
- Civil litigation required to impose monetary sanctions (except for reporting violations)

Management Process

- National policy priorities established on an annual basis
- Regional office given budget and operational targets
- Broad discretion provided in individual case selection and resource allocation
- Automated data and case selections tools provided
- Quality and policy review at multiple levels

Basic Strategies

- Reliance on deterrence
- Leverage limited resources
- Focused Agenda - Strategic Case Selection
- Voluntary Compliance & Assistance
- Mandatory Indemnification/Insurance
- Outcome oriented measurement and evaluation

Credible Deterrence

- Comprehensive Reporting Structure
 - Periodic Financial and Operating Reports
 - Individual Accounts Balance and Benefits
 - Public Disclosure of Reports
 - Reporting Enforcement Program
 - Automation of Reported Data
- Consistent Application of Sanctions
- Publicize Enforcement Actions

Leverage Limit Resources

- Cooperative/Referral Arrangements With Other Authorities (Banks, Insurance, Securities Markets)
- Focus on Major Service Providers/Financial Institutions to Multiply Access to Funds
- Utilize Independent Auditors to Identify Potential Problems
- Facilitate Public Access to Supervisor to Enhance Case Identification and Selection

Strategic Agenda Setting

- Annual Identification of Major Issues
- Rotating Focus Specific Issues to Maximize Impact
- Coordinate Agenda With Regulatory Issues and Broader Market Conditions

Technical Assistance & Education

- Outreach and Technical Assistance to Prevent Violations of Standards
 - Publications and Seminars
 - Internet Based Resources
- Strategic Partnerships With Relevant Industry Groups
- Participant Education of Rights
- Identification of cases from interactions with public

Voluntary Compliance

- Structured Program of Voluntary Agreements/Settlements
- Incentives for Self Correction of Violations
 - Relief from Monetary Penalties
 - Waiver of Admission of Violations in Specifically Defined Circumstances
- Cohesive Program to Publicize Imposition of Sanctions

Indemnification and Insurance

- Mandatory Bonding or Prudential/Fiduciary Insurance
- Required Involvement and Liability for Custodians and Auditors
- Knowing Participation and Joint liability Standards
- Access to “Deep Pockets”

Outcome Measurement & Evaluation

- Outcome Rather Than Process Oriented Performance Objectives
- Integrated Strategic Planning and Outcome Evaluation
- Sampling and Inferential Methods to Establish Baseline & Intervention Impacts
- Alignment of Management Evaluation and Incentives With Strategic Objectives

Reasons for Approach

- Voluntary System – Tension Between Security and Coverage
- Low Resource Levels Relative to Scope of Responsibilities
- Regional Diversity in Types of Funds and Service Providers
- Variation in Interpretation of Statute by Jurisdiction
- Strong Regulation of Primary Financial Products
- Tradition of Individual Civil Litigation and Exercise of Rights

Major Challenges

- Political Acceptance Of the Inability To Address All Violations
- Resource Rationing
- Sustaining Strategic Objectives
- Policy Consistency Over Time and Among Regions
- Reconciling Conflicts With Other Regulated Sectors